

NIE : IRAN

CONTENTS

	Page
PRECIS	1
DISCUSSION	4
I. DOMESTIC POLICIES AND PROSPECTS	4
The Shah	4
The Institutional Context	5
Supporters and Challengers	6
A Contingency: The Shah's Demise	7
II. NEAR-TERM ECONOMIC OBJECTIVES AND OUTLOOK	8
Outlook	9
Implications for the US	10
III. MILITARY DEVELOPMENTS	10
IV. IRAN'S FOREIGN RELATIONS	12
The Shah's Perspectives	12
The Persian Gulf and the Arabian Peninsula	12
Iraq	13
The Middle East	13
The Indian Ocean	14
CENTO	14
The USSR	14
China	14
Relations with the US	14
Problem Areas	15

SECRET

IRAN

PRÉCIS

A. We see little prospect during the next few years for a serious challenge to the Shah's authoritarian control over Iran's internal affairs and programs. Nevertheless, the Shah's monopoly of decision-making and his trend toward greater repression of opposition will incur certain political costs:

- growing alienation and dissent, including terrorism, on occasion with anti-US overtones;
- limited bureaucratic and governmental effectiveness in implementing the Shah's ambitious objectives;
- the stifling of political institutions which could maintain stability after the Shah's demise.

B. The Shah is unlikely to change his course materially; hence strains within Iranian society seem destined to grow as other sectors of life modernize and the pressure for political participation becomes more insistent. In the event of the Shah's early death, competition for power could lead to serious instability.

C. In the short run, Iran will be able to obtain the finances necessary to accomplish the Shah's dramatic economic development objectives but will be constrained by:

- an inadequate agricultural base;
- serious shortages of skilled and semi-skilled labor;
- port and transportation bottlenecks.

1
SECRET

As a result, we anticipate a slowdown in the rapid pace of Iran's economic expansion over the next few years. In the longer run, if oil revenues do not rise significantly there will be current account deficits due to increased expenditures in military, industrial, and agricultural products. Even so, Iran will provide opportunities for significant economic gains for the US in investment and trade.

D. By the end of this decade, Iran will have acquired a formidable military arsenal capable of projecting significant ground and air forces into the Arabian Peninsula and South Asia and a blue water navy capable of routine operations in the Indian Ocean. Iranian combat effectiveness, however, will remain limited by lack of training and the ability to maintain sophisticated equipment. Foreign support, particularly from American technicians, will remain essential to Iran's military establishment for many years. The Shah is not likely to seek nuclear weapons in the near future, but he will probably attempt to acquire the necessary technology.

E. The Shah is likely to grow increasingly assertive in his foreign policies. He would risk confrontation with the Arabs, the West, or even the Soviet Union in order to assert Persian primacy in the Gulf or to maintain what he considers a sufficiently high level of oil revenues. Although he will remain suspicious of Soviet intentions and will continue to rely on the US as the ultimate deterrent to the USSR, the Shah believes he has taken out insurance in the form of economic and political ties and that he can deal effectively with the Soviet Union on his own under foreseeable circumstances.

F. Iran will be prepared to deploy forces unilaterally in order to forestall a radical upset in the Gulf. There are also prospects for greater cooperation with Saudi Arabia's Prince Fahd and, following Iraq's recent regional overtures, for a reduction in Iraqi-Iranian hostility. Iran's relations with South Asia will remain limited over the short term; the Shah is likely to limit his financial backing for Pakistani arms purchases. In the Middle East, the Shah will probably continue to expand his relations with Egypt, and it is becoming less likely that Iran would supply Israel with oil in the event of resumed hostilities.

G. US-Iranian relations are likely to become more difficult in coming years. The Shah is seeking to remove both the US and Soviet military presence from the Persian Gulf and the Indian Ocean and to establish his own regional collective security arrangements in the Gulf; while he will tacitly approve of US naval operations in these waters as

SECRET

long as the USSR keeps naval vessels on station there, we cannot depend on him to provide access to Iranian facilities to support fleet units, and he will probably use his influence to end our use of Bahrein.

H. Specific problem areas include:

- the Shah's efforts to maximize oil prices and the buying power of oil;
- arms procurement and the pressures that the Shah may levy to ensure his perceived military and security requirements are met;
- the growing number of Americans in Iran, expected to reach about 50,000 by 1978;
- Arab-Iranian rivalries forcing the US to choose sides;
- the question of safeguards for nuclear equipment and fuels.

I. The Shah's strategy in dealing with the US is likely to continue to be based on efforts to expand economic ties with the US to offset strains developing from his growing political independence. He provides important intelligence facilities for use against the USSR and would probably cooperate in facilitating US political initiatives in Middle Eastern diplomacy. While over the short term, US and Iranian interests are likely to be largely compatible, we can no longer rely on the Shah to accommodate US interests in the increasing number of areas where his interests diverge from ours.

J. While US-Iranian relations would come into question if the Shah should leave the scene, much of the relationship has become institutionalized to the point where it transcends the Shah. Power would rest at least initially on a military-bureaucratic coalition, but they would come under increasing pressure and we cannot now foresee the nature of the regime which will ultimately succeed the Shah. But even a more extreme regime probably would not immediately seek to restructure the present relationship in drastic ways given the Iranians' view of their interests and the importance of the US connection.

SECRET

SECRET

DISCUSSION

I. DOMESTIC POLICIES AND PROSPECTS

The Shah

1. In Iran today, the state and the Shah are virtually one. The Shah has succeeded in concentrating power and decision-making firmly in his own hands. In the process, he has removed or neutralized every official who might challenge him and has stifled the capacity of the political system to act without him. Thus to understand the Iranian political system one must understand the personality and character of the Shah himself.

2. Since his earliest years, the Shah has been imbued with a sense of specialness. This has been translated into his mission to modernize his country economically and militarily so that he and Iran can play a major role in world affairs and dominate the Persian Gulf. Proud of his image as a royal revolutionary, he has been directing the "White Revolution" for over a decade to transform Iran into a modern state. To the Shah social justice means primarily closely-supervised economic development to raise the living standards of the masses. He regards Iran's growing prosperity as an essential antidote to pressure for far-reaching political transformation.

3. The Shah has no intention of sharing political power. He views Iranian politicians as by nature fractious and uncooperative and prefers to work

through a small coterie of loyal and tested assistants. His willingness to tolerate limited party competition stemmed from the desire to appease critics in the West and among Western-influenced elements of the population. But he has long been mistrustful of the parliamentary process. In his view, representative government is at best a distant goal suited for a successor, although he feels defensive about the anachronistic appearance of absolute monarchy in the last quarter of the 20th Century.

4. The Shah is a man in a hurry. He is only 55 years old and is in good health. But he appears to fear that unless he impels Iran much further along the path of modernization, his successor will be unable to sustain the momentum. His urgency is also stimulated by the conviction that Iran must develop before its oil runs out or the value of its oil is undercut by alternative sources of energy. The forced-draft nature of all his projects suggests that he has a deadline in mind. The Shah probably wishes, by staying ahead of demands for changes, to move fast enough that when his son comes of age six years hence Iran will be at the point of self-sustaining development. This concern may be evidenced in the Shah's remark last year that while the Crown Prince could do much good as king in the future if he were willing, "we are fixing things so he can do no harm."

SECRET

5. In this situation, the Shah will not give up his exclusive responsibility for all major and many minor decisions. If anything, this method of operation is likely to become more pronounced. Particularly since his celebration of the 2,500th anniversary of the Persian monarchy, his sense of infallibility has become more apparent and he has become more isolated from opposing views. Several recent major decisions appear to have been taken by the Shah with little consultation even with his coterie; for example, the creation of a new single-party system, and the agreement with Iraq at the expense of the Kurds. The Shah seems likely to make more decisions without reference to his advisers. While his judgment has proved generally sound thus far, and is likely to continue so, nonetheless, his monopoly of the decision-making process inhibits the development of institutional mechanisms and imposes an even greater burden on his energies and wisdom.

The Institutional Context

6. In Iran, politics revolves around personalities and cliques, not formal associations and institutions. Parties, cabinets, and parliaments are merely the stage on which these cliques interact. The crucial questions, therefore, center on the quality and competence of particular individuals, the position of these individuals vis-a-vis the monarch, and the coalitions and rivalries among these cliques.

7. The most important political clique in Iran is the coterie of individuals surrounding the Shah. This group consists of a dozen old classmates, trusted advisers, loyal military and civilian officials, and relatives. A key figure is Empress Farah, the mother of and designated Regent for 14-year-old Crown Prince Reza. Although the other members of the inner circle remain deferential to the monarch and isolated from the rest of Iranian society, the Empress, his own private network of informants and consultants, and SAVAK (the national intelligence organization), are his principal means of keeping in touch with developments in Iran. The Empress has a reputation for integrity unusual for

the inner circle and enjoys considerable, although diminishing, respect among educated Iranians.

8. Cliquishness, personal insecurity, and inertia dominate the Iranian bureaucracy. While the Shah recognizes that these traits have hampered the implementation of his policies, the administrative transformation mandated by the White Revolution has foundered on the Shah's own reluctance to reward individuals who display initiative, efficiency, and judgment. The first requirement of Iranian administrators is loyalty; the higher one climbs up the bureaucratic ladder, the greater the salience of this factor. Consequently the higher levels of the bureaucracy have come to be stocked with technocrats and administrators who choose bureaucratic survival over accomplishment. Corruption is endemic but is no worse than in other countries in the region. Bureaucratic inefficiency will delay some of the Shah's programs and to that extent will frustrate the expectations of both the Shah and the people. We do not expect significant improvements and the government will face increasing administrative challenges.

9. Political party activity in Iran has no autonomous life. The Iran Novin Party was designed to mobilize mass support and to provide a channel for limited feedback to those in power. It became instead a collection of competitive cliques directed by Prime Minister Hoveyda. Elections, parliamentary debate, and shifts of personnel were inconsequential to the actual course of developments. The existence of the loyal opposition, the Mardom Party, however, provided an appearance of political competition which permitted a number of Iranians to rationalize their participation in the Shah's system.

10. The replacement of this structure by a single party last March represents no change in the basic machinery of political decision-making. The creation of the Iranian National Resurgence Party shows that the Shah has lost interest in the facade of competitive politics. The new party, run by the old group of politicians headed by Hoveyda, appears to have little potential for mobilizing grassroots support for the regime. The Shah rejected the previous notion of a loyal opposition as a

SECRET

SECRET

vehicle for expressing a variety of opinions and thereby has reduced the ability of the system to accommodate differing points of view.

11. If, as we believe likely, the new party fails to deal with dissent and to provide greater outlets for the demand for political participation, strains within Iranian society will increase. The Shah is unlikely to act on his declaration that all who do not join the new party should face jail or expulsion from the country. More likely, he will use party membership as just one of the many criteria for allowing participation in the system. He will continue to rely on SAVAK to manage and control political activity from behind the scenes. In so doing, the Shah is counting on the flexible and resilient nature of the Iranian social system which has traditionally allowed the ambitious to become influential as long as they played by the rules established by the ruler. But the operation of this system breeds widespread personal insecurity and cynicism which discourage voluntary cooperation and national commitment. As a result, some capable Iranians will increasingly be left on the sidelines, benefiting materially from the development process, but assuming no responsibility for the success of the Shah's program.

Supporters and Challengers

12. Only rough assessments are possible on the extent of support for the Shah. Opposition sentiments are taboo in public and expressed in private only with great discretion. The bulk of the population, mostly peasants, has been traditionally apolitical; it generally has supported the monarchy as an institution, although not necessarily any specific monarch. The peasants have gained in absolute terms from the reforms, but there is no indication that their higher standard of living has been translated into support for the Shah.

13. The major source of strength for the Shah has been his military and security forces. The Shah takes particular care to keep his officer corps content, mostly through the provision of extensive perquisites such as salaries and housing. However, the increasingly high level of education required

by the modernizing of the Iranian military forces may affect the political reliability of the officer corps. Present commanders, like their civilian counterparts, are selected primarily on the basis of loyalty to the regime. Those at the top of the military establishment today are not particularly competent. As better educated officers, who are more likely to have imbibed some of the intellectual dissent of their civilian peers, come into middle-grade positions, it will become more difficult for the top-ranking generals to maintain their present tight control.

14. The most wholehearted backers of the Shah are those few thousand who profit personally from close association with the Court; they would also suffer most if the system were eliminated. Besides the inner circle of the Shah's principal assistants, this group includes bureaucrats, cronies, hangers-on, and business and professional men whose importance arises from their access to the Court advisers.

15. A far larger group—administrators, middle-class professionals and probably even the bulk of the urban lower class—go along with the Shah not so much out of conviction but because they have profited from the system and do not see an alternative. Unenthusiastic about the Shah as a person, many perhaps even unenthusiastic about the monarchy as an institution, most of this group would probably switch loyalties easily as long as they perceived no threat to their personal interests. This lack of enthusiasm leads to considerable passivity, and the services of many upper-class, experienced administrators are denied either by their own choice or by what the Shah considers their political unreliability.

16. Prominent in the opposition are the religious leaders and through them the religious establishment. They have longstanding objections to reform-minded monarchs and a particular antipathy for the Pahlavi dynasty. Religion has been a major influence among the urban lower classes and the bazaar merchants. Even the intelligentsia, who in other circumstances would be scornful of the religious establishment, now apparently perceive the religious leaders as sharing common grievances against the present system.

SECRET

17. Opposition to the Shah and his regime is entrenched among intellectuals. Writers, poets, and artists, who traditionally have played an important role in Iranian political life, are contributing to the emergence of a class of alienated intellectuals. Their demands for political participation and freedom of press and expression have no place in the White Revolution. The Shah's style of government forecloses relaxation of police repression and an end to corruption desired by this opposition. Educational excellence and administrative efficiency did fall within the Shah's program, but he has deplored the lack of effective action in these fields. Student unrest is endemic. There seems almost no chance that the Shah's regime, however successful in material terms, will be able to satisfy these elements. Their desire to share political power is more troublesome for the Shah than the nationalist demands of reformers of the Mossadeq era who have been satisfied merely to participate in the process of economic development.

18. Intellectual dissent has produced a climate in which acts of terrorism are increasing. Ideologically, the extremists range from anarchist-communist to the radical religious right, but they are principally interested in violence against the regime. This accounts for the seeming anomaly of terrorists financed by merchant money and espousing a combination of Islamic and Marxist principles. In the past two years, members of several small extremist organizations have been responsible for at least ten assassinations and a score of bombings. Their main aims appear to be to demonstrate the inability of the security forces to prevent their activities, to eliminate security officials who have been a danger to them, and to force the security forces into actions which would arouse widespread popular resentment. On occasion, terrorism will spill over and become directed against the US and US-sponsored activities.

19. Although individual acts of violence are likely to increase, they pose no immediate threat to the regime. The security forces have had considerable success in detecting and breaking up individual cells. The agreement with Iraq may

have cut off some of the external support for extremist activities. But the growing sophistication of the extremists and their willingness to die for their cause make it almost impossible to stamp out the terrorist organizations. Moreover, they will not lack recruits as long as students and their allies among the intelligentsia remain opposed to the Shah. Indeed, the alienation of these elements is bound to grow, especially as the security forces take an increasingly hard line toward protests of any sort, even when the demands are nonpolitical.

20. As a master political strategist, the Shah will probably seek new ways to head off growing discontent. He may announce new welfare programs to bring tangible benefits to the masses. He may attempt further political rearrangements to infuse greater vigor into the Iranian National Resurgence Party. But the main lines of his policy seem already laid down and will not accommodate major political changes. Hence, strains within Iranian society seem destined to grow as other sectors of life modernize and the pressure for political participation becomes more insistent. Nonetheless, we see little prospect during the next few years for a serious challenge to the Shah's total control over Iran's internal affairs.*

A Contingency: The Shah's Demise

21. The Shah's death by accident or natural causes would be less traumatic for the Iranian

*The Assistant Chief of Staff, Intelligence, Department of the Air Force, believes that this Estimate overstates the extent and significance of dissent in Iran and prejudges the Shah's capacity to effect successful reforms. Problems associated with the modernization program in Iran are not necessarily unequivocal danger signs for the regime. The country's economic boom continues to attract many Iranian students back from foreign universities and, while they have indeed absorbed the experience of living in non-monarchical societies, the promise of material reward has proven sufficient to deflect the great majority from political opposition. Nevertheless, the Shah remains cognizant of the need for diffusing political power and responsibility, but he believes that this process must be gradual and need not necessarily reflect Western standards or forms of government. Whether he can be successful in ensuring the smooth transition from a modernizing autocracy to a bourgeois-nationalist constitutional monarchy must therefore remain an open question.

SECRET

system than his assassination. There are probably enough persons with a stake in the established order to ensure continuation of the monarchy, at least in the short run. Although popular, Farah as Regent for Shah Reza would have difficulty in maintaining political stability because of the variety of politicians and military officers jockeying for dominance.

22. Support of the armed forces would be crucial for any succession arrangement. General Khatami, the Shah's brother-in-law and air force chief, would probably be a main prop for the succession, but his relationship with other military officers is not known. While over the years the Shah has exerted great care to weed out disloyal elements in the upper ranks of the military establishment, we do not know how the military commanders would act once he is off the scene. Among the politicians, Prime Minister Hoveyda would have a strong initial position. He has many enemies, however, and would have great difficulty in consolidating his power.

23. The violent removal of the Shah would immediately threaten the system. The Shah is paying increasing attention to his personal safety. While this makes him more isolated and remote, it heightens the chances that his security forces would detect and forestall an assassination which was part of a comprehensive plot to seize control of the government. On the other hand, the Shah's forces still could not be sure of preventing acts by an individual or a handful of plotters willing to sacrifice their lives. If assassins should succeed, the death of the Shah would profoundly shake government officials and the public in general. Under these conditions the senior generals might feel all the more impelled to band together to act swiftly to preserve the system to which they owe so much. But in time they would probably come under increasing pressure from more nationalistic and more radical elements in the middle and lower ranks. Thus the monarchy would face an uncertain future whatever the manner of the present Shah's passing.

II. NEAR-TERM ECONOMIC OBJECTIVES AND OUTLOOK

24. The Shah is embarked on an ambitious restructuring of the Iranian economy over the next decade or so. He is determined to carry out rapid industrialization, capable of supporting a large-scale civilian sector as well as producing late-model weapons systems. Although industrial development is his primary goal, he is willing and able to allocate resources to other sectors which support economic modernization. He recognizes Iran's strong reliance on oil and plans more efficient use of this finite source of wealth. Over the longer term, however, he believes Iran must look to its other resources and, in particular, must transform its poorly educated masses into a nation of skilled laborers and technicians to build a strong industrial base. In the same vein, he proposes to shift the country's energy sources from oil and natural gas to nuclear power. This ambitious program is to be accomplished by injecting massive doses of oil-generated revenues into key sectors with the hope that they will trickle down to provide economic incentive and advancement even for those at the bottom of the social order.

25. The Shah is building on an already fast-growing economic base. Since the mid-1960s, Iran's GNP has grown annually at a real rate averaging 12 percent to about \$40 billion in 1974. The rapid expansion of Iran's oil industry and the application of oil earnings to development have been the dynamic forces behind the rapid growth. Foreign lending which earlier enabled Iran to finance its deficit spending on development and defense was attracted by Iran's oil potential. In some cases, repayments were linked directly to oil or associated natural gas output.

26. In 1974, as a result of the dramatic price rises, Iran's oil revenues quadrupled to about \$20 billion, or roughly half of GNP. The unexpected surge of some \$15 billion was far too great for Iran to devote immediately to economic growth. Of this amount, about one-fourth went for expanded imports, while less than another fourth went for increased domestic development expenditures. The

SECRET

remainder was disbursed in other areas, including loans, and to expand Iran's official reserves which at the end of 1974 were over \$8 billion.

27. The Shah's program for rapid development is creating strains within the economy. By far the greatest problem is a shortage of skilled and semi-skilled workers. The shortage is presently about 700,000 and rising. Introduction of foreign labor, largely from East Asia, can fill only a small part of the gap. Large numbers would greatly add to housing and food supply problems. The 20,000 or so that have arrived are causing resentment among Iranians.

28. There are a number of other problems as well. Port and railhead congestion, resulting from the heavy influx of imports in recent periods, and an inadequate internal transportation network will remain bottlenecks at least in the short term. With production and imports lagging behind the surge in demand, shortages are prevalent, causing significant economic and political problems. There was an inflation rate of about 25 percent in 1974—a serious problem in a country accustomed to nearly stable prices. Iran also is faced with the problem of rising expectations: those who come to the cities from rural areas are unemployed or are relegated to the lower jobs and incomes and cannot find housing or other accoutrements of the "good life" they see around them. There is little hope that the new oil wealth will trickle down far enough or fast enough to prevent growing socio-economic disparities.

29. Agricultural production in recent years has barely kept up with population growth and has fallen increasingly behind the growth in demand. Once a net agricultural exporter, Iran has become increasingly reliant on imports of foodstuffs. In face of a particularly poor harvest last year due to inadequate rainfall, imports grew at least sixfold. Irrigation and other measures to relieve the heavy dependence on erratic rainfall are belatedly being emphasized but have little impact in the short run. More promising in the short term are the efforts to expand rural credit and services. These will not meet Iran's needs, however, and the Shah has in-

dicated that Iran expects to import \$10 billion in agricultural products from the US alone in the next five years.

Outlook

30. Given the problems now confronting the economy, we foresee a slowdown in the rapid pace of industrial expansion and a somewhat lower rate of growth of real GNP over at least the next few years. Many of the projects on the drawing board probably will be deferred or implemented at a slower pace. Military expansion, however, will be largely unaffected by the economic slowdown; the Shah plans purchases abroad averaging about \$5 billion annually over the next five years.

31. Oil will continue to finance Iran's development. Earnings, dependent on production rates and price, are not expected to rise appreciably over the next five years. Iran's oil output is currently about 10 percent below last year's 6 million barrels per day. Although small increases are possible during 1976-77, the longer term outlook is for lower production. Accordingly, oil prices take on increasing importance in the Shah's future revenue plans. He will continue to work for higher oil prices, both making bilateral deals and acting through his leading position in the Organization of Petroleum Exporting Countries (OPEC). He probably will push simultaneously for production limitations to eliminate oversupply and for some form of commodity indexing to protect the value of oil against rising import prices. His allegiance to these policies will find him at odds with the interests of the US and other industrial consuming nations.

32. The Shah's focus on industrial development will include expanded use of oil and natural gas for manufacturing. He is seeking foreign assistance to build oil refineries and petrochemical plants and to market their products abroad. He also is trying to build up markets for Iranian manufactures, partly by tying credits extended to Romania, Egypt and other LDCs to future purchases of Iranian machinery, buses, and consumer goods. Although they should increase rapidly, these non-oil exports cannot replace oil revenues in the foreseeable future. At

SECRET

SECRET

best they will grow from about \$1 billion to \$4 billion in 1980—less than one-fifth of current oil income.

33. Iran's foreign earnings should continue to provide large surpluses for a few years, but thereafter, if oil revenues do not rise significantly, there will be current account deficits. Aware of this prospect, the Shah is adopting restrained lending policies. Increasingly he is attracted to investments which will return badly-needed technology, equipment, and commodities in the coming years. Equities such as those in West Germany's Krupp steelworks are in keeping with this judicious use of current surpluses. This year he acquired a 25 percent share in a West German machinery and construction firm and a 10 percent share in an uranium enrichment plant to be built in France. Loans to the IMF and IBRD further his desire to promote Iran's image and at the same time obtain a respectable return on investment.

Implications for the US

34. The economic and military development under way in Iran provides opportunities for significant economic gains to the US. The US already has the largest investment in and sales to Iran and has favorable opportunities to expand both over the next several years. By 1980 the US investment in Iran could triple to at least \$2 billion. Returns on this investment, as well as repatriation of earnings from the 50,000 US citizens likely to be in Iran by 1980, would be appreciable. Non-oil trade with Iran over the next five years should easily exceed the \$15 billion total mentioned in the earlier Kissinger/Ansari communique and now appears likely to reach some \$25 billion. It would be balanced strongly in favor of the US.

35. Iran's investment and development strategy will also pose problems for the US. Iran is apparently determined to engage in some development whose viability would depend on preferential access to the foreign markets the Shah has been seeking. Iranian exports to third countries under such conditions might affect competing US exports in the late 1970s or early 1980s; increased Iranian production for domestic consumption will certainly

affect certain US exports to Iran itself in the longer run. The Shah's strong interest in US Government participation or involvement in his commercial relations may raise problems for the US. The Shah sees the US Government as a guarantor for the performance of the US private sector and could hold Washington responsible should US industry not meet his expectations.

36. We see, however, little threat to US markets from Iranian export industries in the near term. Iranian exports of non-oil goods will probably not be competitive with US products and will be confined mainly to regional markets in which the US does little business. Military production in Iran will continue to require US and other Western technology and, given the lag in introducing new weapons, will not compete directly with the high value sales of sophisticated US military equipment.

37. Iranian equities in US firms are unlikely to be important from the standpoint of earnings outflow or leverage within any sector of US industry, but may pose problems from the standpoint of industrial firms. Moreover, such equity investment would impose a need on Iran to act responsibly toward the US. Increased Iranian investment in the US would tend to offset risks to US investment in Iran.

38. US sales and proposals will meet increasingly stiff competition from other nations, abetted by an Iranian bureaucracy which is adept at comparison shopping. Furthermore, concern over reliability of supply and fear of being too dependent on any one source will lead the Iranians to disperse projects and purchases widely among the industrial states.

III. MILITARY DEVELOPMENTS

39. Central to the Shah's ambitious plans for Iran's future is the expansion and modernization of the military establishment. Believing that Iran's aspirations as a world power must be based on regional military strength, the Shah is developing a military force stronger than that of any—and all—his neighbors except the USSR. He wants the capability to project military power anywhere in the Gulf area. He particularly desires supremacy over Iraq, which is receiving a continuing inflow of modern arms from the USSR. And he judges that

SECRET

merely a slight edge over all the states in the region is not enough to deter actions hostile to Iran. Finally, he is insistent on acquiring a blue water navy to extend Iranian influence in the Indian Ocean.

40. Iran has been trying to meet these goals since 1968. Military manpower has already increased from about 200,000 to nearly 350,000. The ground forces have been reorganized and reequipped to include three infantry and three armored divisions with over 1,200 late-model tanks. The air force has acquired over 100 F-4s and several ICC-707 aerial tankers. The navy has obtained a large hovercraft fleet and four of the latest model destroyer escorts. The military establishment also includes over 70,000 gendarmes charged with keeping order in the countryside.

41. These forces can do much of what the Shah considers necessary. They are already more than capable of maintaining internal security and of defending Iran's territory against any hostile neighbor but the USSR. Indeed, they have a clear edge in military capabilities over all states in the region and could seize and hold any of the smaller ones on the Arab littoral of the Gulf. But aware of the problems encountered by his expeditionary forces in Oman, the Shah recognizes that in practice their performance leaves something to be desired.

42. The Shah hopes by acquiring additional quantities of the latest-model weaponry to overcome present deficiencies and keep far ahead of Iraq's continuing military modernization. He plans to expand his armed forces by another 50,000 men to nearly 400,000 by 1978. Much of this growth is in conventional ground forces, where the scheduled acquisition of over 400 additional helicopters designated for troplift and attack roles will give the Shah a major offensive capability. He will bolster Iranian naval power by purchasing the most modern destroyers, additional hovercraft, submarines, and anti-submarine aircraft; he appears to be preparing eventually to add some type of aircraft carrier to the fleet. By 1980 the Iranian air force should have nearly 24 fighter-bomber squadrons of over 400 late-model aircraft, including 80 F-14s with associated Phoenix missiles.

43. The new weapons for this force will cost at least \$25 billion over the next five years. One of the considerations motivating the rapid buildup is the Shah's desire to avoid future price rises by purchases at today's lower cost. Thanks to the current high oil prices, Iran has the funds to purchase the military equipment the Shah desires and to set up the factories necessary for the military industry he now envisages.

44. To reduce Iran's total dependence on foreign suppliers for the sophisticated weapons systems he desires, the Shah wants to coproduce late-model weaponry in Iran under license, mostly in conjunction with US firms. Coproduction will not significantly lower the cost of these weapons, and is likely to increase it somewhat. The Shah, however, believes it will give Iran a more dependable source of supply. Much of this gain is illusory, however; components for the more sophisticated items will still have to be imported, though it may be easier to purchase parts on the world market than to procure the entire weapons systems.

45. Iran has the financial resources to carry out its ambitious military modernization program without cutting severely into development projects. Nevertheless, the expansion and upgrading of the armed forces, by increasing the pressure on the limited pool of skilled manpower, may inhibit growth in the developmental sector. The competition for manpower poses a difficult problem of priorities for the Shah, who is deeply committed to both economic development and military modernization.

46. Deliveries of sophisticated military equipment will increase Iran's dependence on foreign technicians. Even if foreign technicians reach currently projected levels—perhaps as many as 15,000 by 1980—lack of trained manpower will seriously impair operational effectiveness of the armed forces over the next several years. Indeed, it will be a long time before the Iranians can use on their own the complex weapons systems they have begun to acquire.

47. The largest group of these foreign technicians will be Americans, who already number about

SECRET

4,000. The US is committed to supplying and, in some cases, coproducing advanced weapons systems; it is also committed to training Iranians in their use. By 1978 foreign personnel will make up a significant proportion of all Iranian support and maintenance personnel. Moreover, the US will be deeply involved in building a blue water navy, maintaining and supporting tactical and support aircraft systems, and establishing communications systems.

48. The Shah's preoccupation with keeping ahead of regional rivals raises the question of his intent to develop nuclear weapons. Iran is a party to the nuclear non-proliferation treaty and has also proposed a UN resolution calling for the establishment of a nuclear weapons free zone in the Middle East. But India's nuclear testing program is probably giving the Shah second thoughts about Iran's renunciation of nuclear weapons. Moreover, his proposed nuclear power program would give him some of the essential elements needed to develop the weapons. The facilities needed for the domestic production of fissionable material, however, would require extensive foreign assistance. The time required to build and operate these facilities would depend on the priority given and the amount of foreign assistance provided. In any event, it would take at least a decade to overcome these basic deficiencies.

49. The Shah would like to move toward a position where he could eventually produce nuclear weapons on short notice if he believed it necessary. Nevertheless, in view of the difficulties in developing the facilities needed to produce such weapons, he does not seem likely to decide to launch a nuclear weapons program in the near future. We can expect, therefore, that Iran over the next decade will make a major effort to acquire facilities and develop the know-how and technology to manufacture nuclear weapons, but without taking a firm decision to undertake actual production. The Shah would hope that by avoiding a definite program to produce nuclear weapons he would forestall problems with the US over his nuclear intentions.

IV. IRAN'S FOREIGN RELATIONS

The Shah's Perspectives

50. Basing his foreign policy on a historical perspective, the Shah is acutely conscious of the contrast between past Persian glory and present Iranian reality. He sees Iran confronted by an untrustworthy Soviet Union, while he sees the remote bastions of Western power in a state of disarray and decay. Although he would count on US support in a confrontation with the USSR, he has taken out insurance in the form of economic and political ties with the Soviet Union and does not feel himself directly threatened from that quarter. Massive oil revenues give him confidence that he will be able to secure whatever military and industrial equipment he considers necessary. Against this backdrop, the Shah will seek:

- domination of the Persian Gulf;
- a preeminent role in OPEC;
- the extension of Iranian air and naval power into the Indian Ocean;
- expansion of Iranian influence in the Middle East, Europe, Asia, and Africa.

51. He would accept confrontation with the Arabs, the US, or even the Soviet Union if necessary to assert Persian primacy in the Gulf or to maintain what he considers a sufficiently high level of oil revenues; in other matters and areas he is likely to be more cautious. The Shah's past behavior has reflected a relatively realistic appreciation of Iran's capabilities and of the interplay between regional and international power. But as he grows older and more convinced of the soundness of his own judgment and as Iran's military strength increases, he is likely to take greater risks to achieve his ambitions.

The Persian Gulf and the Arabian Peninsula

52. The Shah sees the Persian Gulf as studded with inept backward regimes susceptible to radical subversion. To deal with this danger, he is proposing a regional collective security arrangement.

~~SECRET~~

While the Shah hopes that Saudi or other Arab elements will prevent or suppress radical movements on the Arabian Peninsula, he will be prepared swiftly to deploy Iranian forces across the Gulf to forestall a radical upset. He would prefer to act in concert with the conservative Arab states, or at least on invitation of a beleaguered regime—as in Oman—but would not wait for Arab agreement if he considered Iran's interests at stake. The Shah recognizes Arab suspicions and anti-Persian sentiment and will seek where possible to avoid an unnecessary confrontation. However, with the 1971 seizure of the Tunbs and Abu Musa Islands as a background, Iran is likely to take further unilateral action in the Gulf if it perceives a potential threat to its regional hegemony.

53. Iran will probably have more possibilities for cooperation with Saudi Arabia now that Faysal is off the scene. Prince Fahd, who appears to be the real power in the Saudi monarchy, is likely to be less rigid and more open in dealing with Iran than Faysal was. On the other hand, even the present climate of good feeling cannot completely allay the traditional mistrust of these historic rivals in the Gulf. Hence, coordination between Iran and Saudi Arabia will be difficult, and actions will often be complementary rather than taken in concert. The potential for conflict of interest will remain high. On balance, however, we believe that both states will be alert to this danger and we do not foresee insuperable differences arising during the next few years.

Iraq

54. With the Algiers accord of March 6, Iraqi-Iranian relations moved from the brink of hostilities toward a semblance of coexistence. The accord eliminates the Kurdish problem and the disputed Shatt al-Arab river border as immediate sources of conflict. The Kurdish drive for autonomy in Iraq appears to have been effectively crushed and, following its abrupt abandonment of the effort, Iran probably could not revive Kurdish opposition for some time.

55. There are, however, traditional antagonisms and long-standing basic differences that cannot be swept aside overnight. Iran sees Iraq as a potential threat, especially by virtue of its Soviet-equipped armed forces and the Soviet military presence there. Baghdad, for its part, fears Iranian hegemony in the Gulf backed by massive arms purchases from the US. Moreover, the Iraqi Baathist regime and the Iranian monarchy remain the antitheses of each other. Yet recent Iraqi moves raise the possibility of a fundamental revision of Iraq's approach to the Gulf. Relations between Iran and Iraq, therefore, may be less volatile than in recent years and there appears some prospect of gradual improvement and more stability in this relationship.

The Middle East

56. Events since the 1973 Arab-Israeli war diminished Iran's traditional aloofness toward the Arabs and weakened covert cooperation with Israel. While Iran's new Arab posture extends to Syria and Algeria, it centers on Egypt and seems to provide for a certain amount of cooperation between Cairo, Jidda, and Tehran. The major considerations for Iran's shift appear to have been Sadat's moderation, his growing leadership of the Arab cause and his ability to negotiate directly with the US. Iran's opening toward Egypt also facilitates cooperation with Saudi Arabia. These trends seem likely to continue.

57. While the Shah continues to welcome Israel as a strong pro-Western and anti-Communist balance to Arab nationalism in the Middle East, he sees Israel as a diminishing asset. He recognizes that a continuing Arab-Israeli impasse encourages the growth and unity of Arab radicalism. He has also noted the lessons of the 1973 war—the difficulty of US access to Israel, the retreat of European support, and the growing risk of a US-Soviet confrontation because of Arab-Israeli hostilities. Iran is not likely to turn against Israel and will probably continue oil shipments and covert intelligence exchanges. In the event of resumed hostilities, however, we cannot be confident that Iran would continue to supply Israel with oil.

SECRET

The Indian Ocean

58. The Shah wants Iran to be a leading—if not the dominant—power in the Indian Ocean. Seeing India as a major potential rival in this region, he has recently stepped up efforts to improve relations with India in order to reduce the likelihood of friction. Iran is seeking raw materials from India and will probably supply a major portion of India's fuel requirements at manageable prices at least for the next few years. The Shah has also begun cultivating conservative, pro-Western governments such as Australia, New Zealand, Indonesia, Singapore, and South Africa, but in low key to avoid irritating the nonaligned states. Over the longer term, the Shah will work for the elimination of both Soviet and US military presence in the Indian Ocean. While he will tacitly approve a US naval presence as long as the Soviets keep naval vessels on station there, we cannot depend on him to provide access to Iranian facilities to support fleet units.

CENTO

59. The Shah regards his CENTO alliance with Turkey and Pakistan as a useful adjunct to his regional policy. He is concerned about the possibility that Pakistan and Afghanistan might come to blows over their volatile tribal populations, a conflict he fears would spill over into Iran's tribes as well. He is also mistrustful of the course of Indian relations with Pakistan. Despite his concern, the Shah is likely to weigh carefully and limit his financial backing for Pakistani arms purchases. While he might provide Bhutto some equipment if Pakistan were threatened by its neighbors, Iran would probably not become involved in hostilities in support of Islamabad except perhaps in the event of unprovoked Indian attack. As for Turkey, the Shah's sympathies for its efforts to circumvent the US arms embargo are strong, and he might permit some "leakage" of spares to Ankara, but would be circumspect in order to avoid risking relations with the US.

The USSR

60. The Shah has no doubt that Iran's natural and most vital interest is with the West, but he regards

normal, if cautious relations with the USSR as necessary to permit freedom of action in pursuing his goals. By expanding trade with the USSR and by regular high-level political exchange, he believes he has provided strong incentives for Soviet cooperation and has thus reduced the Soviet threat to manageable proportions for the foreseeable future. Indeed, the Shah is now confident of his position. He has already forced the Soviets to accept large increases in the price of gas and introduced surface-to-air missiles into areas of Iraq over which Soviet-piloted aircraft were operating. In short, he still considers the US as an ultimate deterrent to the Soviets but he no longer feels that a US military presence is currently necessary in the region to protect Iran and he believes that he can deal effectively with the Soviet Union on his own. Moscow, for its part, is unlikely to take action in the Gulf area which would risk its good relations with Iran, and probably sees little alternative but to tolerate the Shah's increasing assertiveness.

China

61. Relations with China have been relatively inactive since Iran's recognition of Peking in 1971. Both countries share a strong interest in blocking the spread of Soviet influence in the Middle East and South Asia. China has endorsed Iran's military buildup and, apparently at the Shah's behest, terminated its support for the Dhofar rebellion. For its part, Iran sees China as useful to balance its relations with the Soviet Union and the US. While we do not envisage a rapid strengthening of Sino-Iranian relations over the near term, we would expect a growing mutuality of interests and a continuation of exchanges of high-level visits including, perhaps, a trip to Peking by the Shah.

Relations with the US

62. The Shah is ambivalent in his view of the US. On the one hand, he believes US interests in Iran are sufficiently great that he can rely on US support in a confrontation with the Soviet Union. Moreover, he counts on the essential compatibility of basic US and Iranian interests and regards the US as the

only practical source of late-model weapons and industrial goods he believes necessary to turn Iran into a world power. On the other hand, he is concerned that the US may not be able to resolve its own foreign and domestic problems. He wants to be as independent of the US as possible and would like to see the US role (as well as that of the USSR) in the Gulf reduced or eliminated. Indeed, he even is going so far as to inspire increasing press criticism of US foreign policy, at least in part to drain lower and middle class opposition away from himself by portraying himself as a progressive nationalist fighting American economic imperialism.

63. The Shah's primary strategy to assure continuing military supply involves seeking to deepen ties with the US. He hopes by offering lucrative and tempting economic deals to make certain that Washington would find it inexpedient to turn down his future requests. He is also actively wooing American educational institutions, at least partly in order to improve Iran's image in the US, and is participating in a series of joint commissions to concert efforts to develop Iran in economics, social welfare, and culture. He has long provided important intelligence facilities for use against the USSR. He would probably cooperate in facilitating US political initiatives in Middle Eastern diplomacy. In taking such decisions, he will pursue what he considers Iran's basic interests and we cannot rely on him to accommodate the US in the increasing number of areas where his interests are expected to diverge from ours.

Problem Areas

64. Expanding and deepening relations with an increasingly unpredictable and assertive Shah will create vexing problems for the US. In the first place, he is likely to be a very tough bargainer in pressing to meet what he considers his vital military and security requirements. He believes Iran's oil money, its relative pre-eminence in the region, the stability of his regime, and—not least—the soundness of his own judgment give him high cards to play with the US. While in the final analysis he would avoid a showdown that would damage his ties with Washington, he generally has little fear of pressing his

case too far. As a tactic to extract firmer American guarantees of performance, he will question US reliability as a supplier, citing the experience in Pakistan, Indochina, and Turkey. He also may from time to time raise the possibility of turning to Europe as an alternative to the US, though he probably does not regard this as a practical option for large-scale procurement, especially of weapons systems.

65. Rapid growth in the numbers of American personnel to service the multiplicity of projects which this expanding relationship entails also carries potential for trouble. At the very least, it raises the prospect of a multitude of problems in cultural adjustment and intercommunal relations. With nearly 50,000 American civilians (including dependents) assisting in the Shah's program by 1978, the chances of friction in the relationship would undoubtedly grow. More serious would be the risk of involving US personnel in roles supporting Iranian military action in the event of regional conflict. The accord with Iraq diminishes the prospect of hostilities over the next few years. But the inability of Iranians to operate all the late-model equipment Iran will acquire in this period poses a continuing concern.

66. Oil policy forms an area where collisions between the Shah and the US are all but inevitable. The Shah has already proved quite adamant in refusing to cooperate to secure oil price reductions. His interest in receiving the maximum return for oil is so intense that he is likely to continue to take the lead in urging continual increases in oil prices in order to maintain at least the present relative advantage of Iranian purchasing power. Though he will seek to keep the image of reasonableness and moderation as a bargainer in petroleum matters, the Shah will thus be likely to run afoul of US interests in oil questions as he seeks to maximize his income.

67. The Shah's regional policies also carry risk of conflicting with US interests. This is particularly true of the Gulf, where the specter of Iranian military power increasingly will alarm Iran's neighbors. Thus far, the Shah has been relatively judicious in his actions. He has been particularly aware of Arab sensitivities in providing troops to assist the Sultan of Oman, and we would expect

SECRET

him to continue to act with restraint. But the Shah has little respect for the capability of the leaders of neighboring Arab states. As he boosts his Gulf forces and finishes construction of naval facilities over the next few years, the opportunities for falling into more overt rivalry with Saudi Arabia will grow.

68. Even the Shah's desires for economic development raise issues that will be troublesome to resolve. For example, his ambition to purchase from the US a large-scale net of nuclear generating plants to supply Iran's future power requirements poses potential problems. For reasons of national pride and to keep his options open, the Shah is reluctant to agree to US demands for safeguards for these reactors more stringent than those imposed by IAEA; this reluctance is unlikely to abate. As in other matters, he will seek to hold the Executive Branch responsible for bringing the Congress along behind this deal with Iran. In this situation his nuclear program may become a continuing thorn in US-Iranian relations as he presses hard to get these plants on his own terms.

69. Underlying these problems is the dependency of the close US-Iranian relationship on the attitudes and perceptions of one man—the Shah. This offers the possibility of an erratic course for personal reasons. More important, it raises questions about US-Iranian relations if he should leave the scene. There is some reason to believe that over the past two decades much of the relationship has become institutionalized to the point where it transcends the Shah. Whether or not the Shah's succession arrangements succeed, power will rest at least initially on a coalition of key military officers and establishment bureaucrats. But this coalition would be likely to come under increasing pressure from diverse elements in society, however, and we cannot now foresee the nature of the regime which will ultimately succeed the Shah. If a more extreme nationalist regime took charge, it might loosen present close political ties to the West, but probably would not immediately seek to restructure the present relationship in dramatic ways, given the Iranians' view of their interests and the importance of the US connection.